

# **REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL LEGISLATURE AND THE COUNCIL ON UMKHANYAKUDE DISTRICT MUNICIPALITY**

## **REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS**

### **Introduction**

1. I was engaged to audit the consolidated and separate financial statements of the Umkhayakude District Municipality, which comprise the consolidated and separate statement of financial position as at 30 June 2012, the consolidated and separate statement of financial performance, changes in net assets and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information, as set out on pages ... to ....

### **Accounting officer's responsibility for the consolidated financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these consolidated and separate financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor-General's responsibility**

3. My responsibility is to express an opinion on the consolidated and separate financial statements based on conducting the audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

### **Basis for disclaimer of opinion**

#### **Property, plant and equipment**

4. The municipality did not assess impairment of non-cash-generating assets at each reporting date in accordance with SA Standards of GRAP, GRAP 21, *Impairment of non-cash-generating assets*. Contrary to the above the recoverable amount was not estimated for all the assets that were damaged at year end. Because of the nature of these assets, it was impracticable to confirm or verify by alternative means the correct value of the non-cash-generating assets. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of property, plant and equipment.

5. The municipality did not account separately for Land and Building in accordance with SA Standards of GRAP, GRAP 17, *Property, plant and equipment*. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the presentation and disclosure of property, plant and equipment.
6. The municipality did not allocate the amount initially recognised in respect of an item of property, plant and equipment to its significant parts and depreciates separately each such part at each reporting date in accordance with SA Standards of GRAP, GRAP 17, *Property, plant and equipment*. Because of the nature of these assets, it was impracticable to confirm or verify by alternative means the correct value of the property, plant and equipment. Furthermore the municipality did not calculate and disclose the prior year depreciation. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the valuation of property, plant and equipment.
7. The municipality did not review the residual values and useful lives of property, plant and equipment at each reporting date in accordance with SA Standards of GRAP, GRAP 17, *Property, plant and equipment*. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of property, plant and equipment.
8. I was unable to physically verify assets to the value of R646,812 million during the audit. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that Property, plant and equipment existed at year end. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself to the existence of Property, plant and equipment.
9. The municipality could not provide sufficient appropriate audit evidence to support additions to Property, plant and equipment to the value of R1,323 million. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that additions had been properly recorded.
10. The municipality did not reconcile a difference of R39,438 million between the financial statements and the underlying accounting records in accordance with SA Standards of GRAP, GRAP 17, *Property, Plant and Equipment*. A difference of R39,438 million exists between fixed asset register and the financial statements. The municipality did not reconcile this difference between the financial statements and the underlying accounting records. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that property, plant and equipment had been accounted for properly. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of property, plant and equipment.

#### **Accumulated surplus**

11. The municipality could not provide sufficient appropriate audit evidence to support prior years' expenses that affected the accumulated surplus of R9,593 million. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that prior years' expenses of R9,593 million had been properly recorded. Consequently I did not obtain sufficient appropriate evidence to satisfy myself as to valuation and completeness of the balance of accumulated surplus.

### **Unspent conditional grants**

12. A material difference exists between the grant register and the financial statements. The municipality did not reconcile this difference between the financial statements and the underlying accounting records. Furthermore the municipality could not provide sufficient appropriate audit evidence to support debit balances for the Municipal Infrastructure Grants amounting to R5,415 million that is included in the notes of prior year financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that grants had been accounted for properly. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of unspent conditional grants.

### **Accounts receivables**

13. A material and pervasive difference exists between the debtors' age analysis and the financial statements. The municipality did not reconcile this difference between the financial statements and the underlying accounting records. Furthermore the municipality could not provide sufficient appropriate evidence supporting the existence of debtors totaling R5,727 million included in the prior year financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that accounts receivables had been accounted for properly. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the existence, valuation and completeness accounts receivables balance.

### **Trade and other payables**

14. The municipality could not provide sufficient appropriate evidence to support journals processed on the accruals account amounting to R8,043 million in the current year. Furthermore the municipality not provide sufficient appropriate audit evidence to support credit balances for trade creditors amounting to R16,983 million that is included in the prior year financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance on validity of these journals. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the existence, valuation and completeness of the balance of trade creditors.

### **Employee related costs**

15. A difference of R13,858 million exists between the payroll records and the financial statements. The municipality did not reconcile this difference between the financial statements and the underlying accounting records. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that employee related costs had been accounted for properly. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the accuracy and completeness of employee related costs.

16. The municipality could not provide evidence supporting the appointment and terminations of employees. There was no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that employee related costs had been accounted for properly. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the accuracy and completeness of employee related costs.

#### **Remuneration of councillors**

17. A difference of R2,699 million exists between the payroll records and the financial statements. The municipality did not reconcile this difference between the financial statements and the underlying accounting records. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that remuneration of councillors had been accounted for properly. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the accuracy and completeness of remuneration of councillors.

#### **Capital Commitments**

18. The municipality could not provide a break-down to support an amount of R191,206 million relating to capital commitments disclosed in note 37 to the financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance on validity and completeness of capital commitments. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the validity and completeness of the amount disclosed as capital commitments.

#### **Unauthorised expenditure**

19. The municipality could not provide a break-down to support an amount of R30,226 million relating to unauthorized expenditure disclosed in note 35.1 to the financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance on validity and completeness of unauthorized expenditure. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the validity and completeness of the amount disclosed as unauthorized expenditure.

#### **Fruitless and wasteful expenditure.**

20. The municipality could not provide a break-down to support an amount of R1,256 million relating to fruitless and wasteful expenditure included in note 35.2 to the financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance on validity and completeness of fruitless and wasteful expenditure. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the validity and completeness of the amount disclosed as fruitless and wasteful expenditure.

### **Irregular expenditure.**

21. The municipality could not provide a break-down to support an amount of R5,421 million relating to irregular expenditure included in note 35.3 to the financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance on validity and completeness of irregular expenditure. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the validity and completeness of the amount disclosed as fruitless and irregular expenditure.
22. Section 125 (2) (d) requires that any particulars of material irregular expenditure to be disclosed in the note 35.3 to the financial statements. The municipality did not design and implement controls to detect irregular expenditure. During the audit of expenditure amounting to R19,507 million was discovered to have been made in contravention of Municipal Supply Chain Management regulations, the municipality subsequently disclosed these payments but did not go back and examine the whole population. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of irregular expenditure as disclosed.

### **Investments**

23. The municipality could not provide sufficient appropriate audit evidence to support a journal processed on the investments account amounting to R110,000 million in the current year. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance on validity of this journal. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the occurrence, accuracy and completeness of the journal processed.

### **Expenditure**

24. The municipality could not provide sufficient appropriate audit evidence to support expenditure items amounting to R20,691 million incurred in the current year. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that expenditure had been accounted for properly. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the occurrence and accuracy of expenditure amount disclosed.

### **Limitation of scope**

25. I was unable to confirm the journals and payments made amounting to R563,349 million and R51,076 million respectively. I could not perform alternative procedures because the supporting documents were destroyed by fire. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the occurrence, accuracy and completeness of the journals and payments made.

### **VAT Receivable**

26. Because of the limitation experiences in the expenditure testing, sufficient appropriate audit evidence could not be obtained as to the valuation and completeness of the VAT receivables as disclosed in the financial statements.

### **Material losses**

27. I was unable to obtain sufficient appropriate audit evidence for the R5,362 million disclosed as water losses in note 46.2 to the financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance on accuracy and completeness of water losses. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the accuracy and completeness of material losses as disclosed.

### **Cash flow statement**

28. Because of the significance of limitation experienced as detailed above, sufficient appropriate audit evidence could not be obtained as to the accuracy and completeness of the cash flow statement as presented.

### **Disclaimer of opinion**

29. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

### **Emphasis of matter**

30. I draw attention to the matter below. My opinion is not modified in respect of this matter.

### **Restatement of corresponding figures**

31. As disclosed in note 34 to the financial statements, the corresponding figures for 30 June 2011 have been restated as a result of an error discovered during 30 June 2012 in the financial statements of the Umkhanyakude District Municipality at, and for the year ended, 30 June 2011.

### **Additional matter**

32. I draw attention to the matter below. My opinion is not modified in respect of this matter.

### **Unaudited supplementary schedules**

33. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited this schedule and, accordingly, I do not express an opinion thereon.

### **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

34. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.



### **Predetermined objectives**

35. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.
36. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the *National Treasury Framework for managing programme performance information*.

The reliability of the information in respect of the selected objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

37. The material findings are as follows:

### **Usefulness of information**

#### **Presentation**

38. Section 46 of the Municipal Systems Act requires the disclosure of measures taken to improve performance in the annual performance report where planned targets were not achieved. Adequate and reliable corroborating evidence could not be provided for all measures taken to improve performance as disclosed in the annual performance report. The municipality records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the validity, accuracy and completeness of the measures taken to improve performance.

#### **Consistency**

39. The Municipal Systems Act No. 32 of 2000 (MSA), section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. The reported targets as included in the service delivery budget implementation plan (SDBIP) or annual performance report submitted for auditing are not consistent with the targets as per the approved integrated development plan. All planned targets specified in the annual performance report were not included in the integrated development plan. This was due to a lack of understanding by business units and inadequate training to enable application of the principles of the Municipal Planning and Performance Management Regulations, 2001.

### **Reliability of information**

40. I was unable to obtain sufficient, appropriate audit evidence to satisfy myself as to the validity, accuracy and completeness of the actual performance reported in the annual performance report. This was due to a lack of a document management system.

### **Additional matter**

41. I draw attention to the following matter below. This matter does not have an impact on the predetermined objectives audit findings reported above.

#### **Achievement of planned targets**

42. Of the total number of planned targets, only 34 were achieved during the year under review. This represents 39% of total planned targets that were not achieved during the year under review.
43. This was as a result of the institution not considering relevant systems and evidential requirements during the annual strategic planning process.

### **Compliance with laws and regulations**

44. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

#### **Annual financial statements**

45. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors were not adequately corrected, which resulted in the financial statements receiving a disclaimer of opinion.

### **Procurement and contract management**

46. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids as per the requirements of SCM regulation 19(a) and 36(1).

### **Expenditure management**

47. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
48. The accounting officer did not take reasonable steps to prevent unauthorised expenditure, irregular expenditure and/or fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.



### **Asset management**

49. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which accounts for the assets of the municipality as required by section 63(2)(a) of the Municipal Finance Management Act.

### **Internal control**

50. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

### **Leadership**

51. The accounting officer did not exercise oversight responsibility regarding financial and performance reporting and compliance with laws and regulations relating to asset management and procurement and contract management.

### **Financial and performance management**

52. Systems and controls were not designed in a manner to prevent, detect and address risks that impact on financial; performance and compliance reporting. In this regard, the accounting officer did not ensure that regular, accurate and complete financial and performance reports were prepared, which were supported and evidenced by reliable information. This resulted in material corrections in financial statements.

### **Governance**

53. The audit committee did not function throughout the year. Members were only appointed four months before year-end.

## OTHER REPORTS

### Investigations in progress

54. Five investigations are being conducted by independent consulting firms on request of the municipality. The investigations were initiated based on the allegations of mal-administration. During the process of these investigations criminal proceedings were instituted against one employee. These investigations were still ongoing at the reporting date.

*Auditor-General*

Pietermaritzburg

13 December 2012



AUDITOR-GENERAL  
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